

§ 1.42-4

whole or in part with funds from an Affordable Housing Program established under section 721 of FIRREA is not, solely by reason of the Affordable Housing Program funds, a below market Federal loan as defined in section 42(i)(2)(D). Thus, any building with respect to which the proceeds of the loan are used during the tax year is not, solely by reason of the Affordable Housing Program funds, treated as a federally subsidized building for that tax year and subsequent tax years for purposes of determining the applicable percentage for the building under section 42(b).

(b) *Effective date.* The rules set forth in paragraph (a) of this section are effective for loans made after August 8, 1989.

[56 FR 48734, Sept. 26, 1991]

§ 1.42-4 Application of not-for-profit rules of section 183 to low-income housing credit activities.

(a) *Inapplicability to section 42.* In the case of a qualified low-income building with respect to which the low-income housing credit under section 42 is allowable, section 183 does not apply to disallow losses, deductions, or credits attributable to the ownership and operation of the building.

(b) *Limitation.* Notwithstanding paragraph (a) of this section, losses, deductions, or credits attributable to the ownership and operation of a qualified low-income building with respect to which the low-income housing credit under section 42 is allowable may be limited or disallowed under other provisions of the Code or principles of tax law. See, e.g., sections 38(c), 163(d), 465, 469; *Knetsch v. United States*, 364 U.S. 361 (1960), 1961-1 C.B. 34 (“sham” or “economic substance” analysis); and *Frank Lyon Co. v. Commissioner*, 435 U.S. 561 (1978), 1978-1 C.B. 46 (“ownership” analysis).

(c) *Effective date.* The rules set forth in paragraphs (a) and (b) of this section are effective with respect to buildings placed in service after December 31, 1986.

[T.D. 8420, 57 FR 24729, June 11, 1992]

26 CFR Ch. I (4-1-08 Edition)

§ 1.42-5 Monitoring compliance with low-income housing credit requirements.

(a) *Compliance monitoring requirement—(1) In general.* Under section 42(m)(1)(B)(iii), an allocation plan is not qualified unless it contains a procedure that the State or local housing credit agency (“Agency”) (or an agent of, or other private contractor hired by, the Agency) will follow in monitoring for noncompliance with the provisions of section 42 and in notifying the Internal Revenue Service of any noncompliance of which the Agency becomes aware. These regulations only address compliance monitoring procedures required of Agencies. The regulations do not address forms and other records that may be required by the Service on examination or audit. For example, if a building is sold or otherwise transferred by the owner, the transferee should obtain from the transferor information related to the first year of the credit period so that the transferee can substantiate credits claimed.

(2) *Requirements for a monitoring procedure—(i) In general.* A procedure for monitoring for noncompliance under section 42(m)(1)(B)(iii) must include—

(A) The recordkeeping and record retention provisions of paragraph (b) of this section;

(B) The certification and review provisions of paragraph (c) of this section;

(C) The inspection provision of paragraph (d) of this section; and

(D) The notification-of-noncompliance provisions of paragraph (e) of this section.

(ii) *Order and form.* A monitoring procedure will meet the requirements of section 42 (m)(1)(B)(iii) if it contains the substance of these provisions. The particular order and form of the provisions in the allocation plan is not material. A monitoring procedure may contain additional provisions or requirements.

(b) *Recordkeeping and record retention provisions—(1) Recordkeeping provision.* Under the recordkeeping provision, the owner of a low-income housing project must be required to keep records for each qualified low-income building in the project that show for each year in the compliance period—